

ORDER NO. 2717

UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Before Commissioners:

Robert G. Taub, Acting Chairman;
Tony Hammond, Vice Chairman;
Mark Acton;
Ruth Y. Goldway; and
Nanci E. Langley

Market Dominant Product Prices
Inbound Market Dominant Multi-Service Agreements
with Foreign Postal Operators 1

Docket No. R2015-5

Hongkong Post—United States Postal Service
Bilateral Agreement (MC2010-35)
Negotiated Service Agreement

ORDER APPROVING ADDITIONAL INBOUND MARKET DOMINANT
MULTI-SERVICE AGREEMENT WITH FOREIGN POSTAL OPERATORS 1
NEGOTIATED SERVICE AGREEMENT (WITH HONGKONG POST)

(Issued September 17, 2015)

I. INTRODUCTION

On August 13, 2015, the Postal Service filed Notice, pursuant to 39 C.F.R. § 3010.40 *et seq.*, of a Type 2 rate adjustment concerning the inbound portion of a bilateral 2015 agreement with Hongkong Post (Agreement).¹ On August 27, 2015, the Postal Service filed workpapers under seal that replace the original workpapers filed

¹ Notice of United States Postal Service of Type 2 Rate Adjustment, and Notice of Filing Functionally Equivalent Agreement, August 13, 2015, at 1 (Notice). The Notice does not contain a copy of the Governors' Decision establishing prices and classifications for the Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators 1 product.

along with the Notice.² The Postal Service seeks inclusion of the Agreement within the Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators 1 (Foreign Postal Operators 1) product. For the reasons provided below, the Commission approves the Postal Service's request.

II. BACKGROUND

Product history. The Commission added the Foreign Postal Operators 1 product to the market dominant product list in Order No. 549, and concurrently included two agreements within that product.³ The Commission has since approved the inclusion of additional agreements within the same product on grounds of functional equivalence, including the predecessor to the instant Agreement, the agreement with Hongkong Post from 2014.⁴

Instant Notice. The Notice includes attachments consisting of an application for non-public treatment of certain materials, the Agreement, and supporting financial workpapers filed in both public and non-public versions.⁵ The Notice includes requests for exceptions to data collection and service performance reporting requirements in 39 C.F.R. §§ 3010.43 and 3055.3(a)(3), respectively. *Id.* at 5-6.

The Notice states that the Agreement results in an improvement over default rates established under the Universal Postal Union (UPU) Acts for inbound letter post

² Notice of the United States Postal Service of Filing Errata Concerning Notice for Type 2 Rate Adjustment and Notice of Filing Functionally Equivalent Agreement, August 27, 2015.

³ See Docket Nos. MC2010-35, R2010-5, and R2010-6, Order Adding Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators 1 to the Market Dominant Product List and Approving Included Agreements, September 30, 2010 (Order No. 549).

⁴ See Docket No. R2014-4, Order No. 1981, Order Approving an Additional Inbound Market Dominant Multi-Service Agreement with Foreign Postal Operators 1 Negotiated Service Agreement (with Hongkong Post), January 29, 2014; Order No. 2286, Order Approving Modification to Existing Agreement, December 12, 2014; and Order No. 2358, Order Approving Modification Two to Existing Agreement, February 18, 2015.

⁵ Notice at 1-2. The full text of the Agreement (signed by the Postal Service) and the supporting financial documentation establishing compliance with 39 U.S.C. § 3622 and 39 C.F.R. § 3010.42 were filed under seal. *Id.*

items and addresses other data and information requirements in Commission rules. *Id.* at 1-7. In addition, the Postal Service states that the Agreement is functionally equivalent to the China Post 2010 baseline agreement filed in Docket No. R2010-6.⁶

The Agreement is intended to take effect October 1, 2015. Notice, Attachment 2 at 7. The Agreement is to remain in effect until December 31, 2016, unless terminated earlier or modified pursuant to the contract terms. *Id.*

Initial Commission action. On August 14, 2015, the Commission issued Order No. 2664 establishing a docket for consideration of matters raised in the Notice, inviting public comment, and appointing a Public Representative to represent the interests of the general public.⁷

III. THE POSTAL SERVICE'S POSITION

Functional equivalence. The Postal Service posits that the Agreement is functionally equivalent to the China Post 2010 baseline agreement (China Post 2010 Agreement). Notice at 7-8. The Postal Service states that the terms of the Agreement fit within the Mail Classification Schedule for the Foreign Postal Operators 1 product and therefore both agreements conform to a common description. *Id.* at 7. The Postal Service also asserts that both agreements are constructed from a similar template; contain many similar terms and conditions; provide rates for small packet with delivery scanning tendered to the Postal Service from each respective foreign postal operator's territory; and are with a foreign postal operator. *Id.*

⁶ *Id.* at 7; see Order No. 549.

⁷ Notice and Order Concerning Type 2 Rate Adjustment and Functionally Equivalent Agreement, August 14, 2015 (Order No. 2664).

However, the Postal Service does identify and summarize differences⁸ that distinguish the Agreement from the China Post 2010 Agreement. *Id.* It asserts that, despite these differences, the Agreement is functionally equivalent to the China Post 2010 Agreement, and that the differences do not affect the cost or market characteristics of the agreements. *Id.* at 9.

Statutory criteria. Under 39 U.S.C. § 3622, the Postal Service asserts that the criteria for the Commission's review are whether the Agreement: (1) either improves the net financial position of the Postal Service or enhances the performance of operational functions; (2) does not cause unreasonable harm to the marketplace; and (3) is available on public and reasonable terms to similarly situated mailers. *Id.* at 6. See 39 U.S.C. § 3622(c)(10).

For the first criterion, the Postal Service provides information in its workpapers showing the expected financial improvements over UPU default rates. Notice at 3. In addition, the Postal Service identifies three improvements that are expected to enhance operational performance: (1) a process for collecting tracking events associated with small packets with delivery scanning sent from Hong Kong to the United States; (2) the establishment of improved accounting and settlement processes; and (3) sortation requirements. *Id.* at 3-4.

Regarding the second and third criteria, the Postal Service contends the Agreement will not cause unreasonable harm to the marketplace, as the Postal Service and Hongkong Post each serves as the respective country's designated operator for the

⁸ The Postal Service lists several differences between the Agreement and the China Post 2010 Agreement concerning inbound rates: the name and address of the foreign postal operator is different throughout; Article 1 of the Agreement differs from Article 1 of the China Post 2010 Agreement; the text of Article 2 and Article 3 differs, slightly; Articles 9, 10, 11 and 13 are different as a result of negotiations between the parties; the Postal Service contact information in Article 15 has been updated; the text of Article 21 and Article 22 is different; the Agreement revises Article 23; the inbound rates and the explanatory terms included in Annex 1 of the Agreement are different; Annex 2 of the Agreement includes an updated reference to a UPU website, a revised paragraph concerning package labeling, a revised "Financial Requirements" section, and additional sortation requirements; the example of a small packet with delivery scanning label in Annex 3 is different; and Annex 5 of the Agreement is different, and includes sortation details specifically relevant to inbound small packet with delivery scanning items. *Id.* at 8-9.

exchange of mail, and there are no other entities similarly situated to serve as designated operators for the relevant types of mail, either originating in Hong Kong or destined for the United States. *Id.* at 4, 6. Also, because no other entities have access to terminal dues rates with respect to inbound small packets with delivery scanning to the United States from Hong Kong sent under UPU documentation, the market for the services offered under this Agreement is, in essence, limited to its parties. *Id.* at 4.

Data collection plan and service performance reporting. The Postal Service intends to report information on the Agreement through the Annual Compliance Report (ACR), and therefore proposes no special data collection plan for the Agreement pursuant to 39 C.F.R. § 3010.43. *Id.* at 5-6. The Postal Service notes, with respect to service performance measurement, that the Agreement is excepted from separate reporting under 39 C.F.R. § 3055.3(a)(3) by virtue of Order No. 996, which established a standing exception for all agreements filed in the Foreign Postal Operators 1 product.⁹

IV. COMMENTS

The Public Representative filed comments on September 14, 2015.¹⁰ No other comments were received.

Functional equivalence. The Public Representative concludes, based on a review of the Postal Service's filing, that the Agreement is functionally equivalent to the China Post 2010 Agreement. PR Comments at 4.

⁹ *Id.* at 6; see Docket No. R2012-2, Order Concerning an Additional Inbound Market Dominant Multi-Service Agreement with Foreign Postal Operators 1 Negotiated Service Agreement, November 23, 2011 (Order No. 996). In Order No. 996, the Commission held that negotiated service agreements with substantially all components of the agreement included in the measurement of other products may be granted and excepted from reporting pursuant to 39 C.F.R. § 3055.3(a)(3). Order No. 996 at 7. The Commission further held that functionally equivalent agreements would qualify for the section 3055.3(a)(3) exception. *Id.* Therefore, agreements that fall within the parameters of the Inbound Market-Dominant Multi-Service Agreements with Foreign Postal Operators 1 product are excepted from the performance reporting requirements of 39 C.F.R. § 3055.3(a)(3). *Id.* at 7, 8-9.

¹⁰ Public Representative Comments on Postal Service Notice Concerning Type 2 Rate Adjustment and Hongkong Post Negotiated Service Agreement, September 14, 2015 (PR Comments).

Statutory criteria. The Public Representative states that while the Postal Service makes reasonable arguments that the criteria relating to unreasonable harm to the marketplace and available on public and reasonable terms are not implicated by the Agreement, he has concerns with regards to the Postal Service's calculation purporting to demonstrate that the Agreement improves the net financial position or enhances the performance of operational functions. *Id.* at 4-5. He asserts that while the Postal Service's financial model appears to meet the criterion, the Postal Service used the 2016 base terminal dues rates for inbound letter post items exchanged between designated postal operators in the target system prior to 2010. *Id.* at 5. He asserts that the Postal Service should have used the 2015 and 2016 provisional quality of service linked terminal dues rates applicable to inbound letter post exchanged between designated operators in the target system as of 2010 and 2012. *Id.* at 5. In addition, he states the term of the Agreement is 15 months, which includes 3 months in 2015. *Id.*

After applying the 2015 and 2016 provisional quality of service linked terminal dues as the default rates in the Postal Service's financial model, the Public Representative concludes the negotiated rates in Hongkong Post 2015-2016 Agreement do "improve the net financial position of the Postal Service." *Id.* at 6 (quoting 39 U.S.C. § 3622(c)(10)(A)(i)).

The Public Representative requests that in future similar dockets, the Commission direct the Postal Service to develop its comparison of the cost coverage at the default rates using the UPU terminal dues rates that would otherwise be paid by the foreign postal operators during the term in which such future agreements would be in effect, assuming the absence of such agreements. PR Comments at 6.

The Public Representative also notes the Postal Service's claim, pursuant to 39 C.F.R. § 3010.42(g), that the Agreement that "should enhance" the performance of mail preparation, processing, transportation, or other functions, is unsupported by evidence or analysis. *Id.* at 7. He concludes the Postal Service does not demonstrate the Agreement meets the requirements of 39 U.S.C. § 3622(c)(10)(A)(ii). *Id.*

V. COMMISSION ANALYSIS

The Commission has reviewed the Notice, the Agreement, the financial analyses provided under seal, and the Public Representative's comments.

Functional equivalence. The Commission finds that the Agreement is functionally equivalent to the China Post 2010 baseline agreement. Differences between the Agreement and the China Post 2010 baseline agreement do not foreclose a finding that the agreements are functionally equivalent. The Public Representative supports this finding. The Commission therefore concludes that the Agreement may be included in the Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators 1 product.

Statutory responsibilities. Under the statutory and regulatory provisions of 39 U.S.C. § 3622(c)(10) and 39 C.F.R. § 3010.40(a), the Commission's approval requires a finding that the agreement either improves the net financial position of the Postal Service or enhances the performance of various operational functions and does not cause unreasonable harm to the marketplace. The agreement also must be available on public and reasonable terms to similarly situated mailers. 39 C.F.R. § 3010.40(c).

The Commission finds that the negotiated rates in the Agreement will improve the net financial position of the Postal Service, as they will generate higher revenues, contribution, and cost coverage than otherwise applicable UPU default rates.¹¹ The Commission also finds the Agreement will not cause unreasonable harm to the marketplace, given the impact of the contracting parties' status as designated operators in the market. The Commission concurs with the Postal Service's assessment that

¹¹ There is insufficient evidence and analysis to support the assertion that it will enhance the performance of various Postal Service operational functions. However, since the Postal Service need only demonstrate that it has satisfied one or the other with regard to "either improve[s] the net financial position of the Postal Service" or "enhance[s] the performance" of various operational functions, a showing that the properly applied rates improve the net financial position of the Postal Service is sufficient to satisfy the first prong of 39 U.S.C. § 3622(c)(10).

there are no entities similarly situated to Hongkong Post, and as such, that criterion is inapplicable.

Although the Commission finds that the Agreement will improve the net financial position of the Postal Service, the Commission agrees with the Public Representative that the Postal Service should have used the 2015 and 2016 provisional quality of service linked terminal dues as the default rates to determine the cost coverage. For future submissions, the Commission directs the Postal Service to ensure that the default rates used to demonstrate improved net financial position under an agreement are, in fact, the rates that would otherwise, in the absence of an agreement, be paid by the foreign postal operator during the agreement's term.

Reporting exceptions. The Postal Service proposes that no special data collection plan be created for the Agreement, essentially seeking a waiver of section 3010.43's data collection reporting requirements. Notice at 5-6. Instead, it intends to report information under the Agreement through the ACR and provide information about mail flows from Hongkong Post within the course of the ACR review process. *Id.* at 5. The Commission finds the Postal Service's request reasonable, and grants the exception. The Commission also approves the Postal Service's invocation of Order No. 996 in support of an exception from separate service performance reporting under 39 C.F.R. § 3055.3(a)(3) on the basis that the standing exception in Order No. 996 continues to apply.

Follow-up submissions. The Postal Service shall promptly notify the Commission if the effective date of the Agreement differs from the intended effective date. The Postal Service shall also promptly notify the Commission if the Agreement terminates earlier than intended or the termination date is modified pursuant to the terms of the Agreement. In addition, within 30 days of the Agreement's expiration date, or early termination, the Postal Service shall file costs, volumes, and revenues associated with the Agreement.

Conclusion. The Commission finds that the Agreement satisfies relevant statutory criteria and approves its inclusion within the Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators 1 product.

VI. ORDERING PARAGRAPHS

It is ordered:

1. The Agreement filed in this docket is included within the Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators 1 product.
2. The Commission approves the Type 2 rate adjustment requested in the Postal Service's August 13, 2015 Notice filed in this proceeding.
3. The Postal Service shall notify the Commission if the effective date of the Agreement differs from the expected effective date identified in the Notice.
4. The Postal Service shall notify the Commission if the Agreement terminates early.
5. Within 30 days of expiration, or upon early termination of the Agreement, the Postal Service shall file related costs, volumes, and revenues data, including any financial penalties.
6. The Postal Service shall, in future submissions with financial models that support a finding of improved net financial position, use default rates that reflect the rates that would otherwise, in the absence of an agreement, be paid during the agreement's term by the foreign postal operator.
7. The Postal Service's request for an exception to the data collection plan requirements under 39 C.F.R. § 3010.43 is granted.

8. The standing exception in Order No. 996 continues to apply with respect to reporting on service performance pursuant to 39 C.F.R. § 3055.3(a)(3).

By the Commission.

Shoshana M. Grove
Secretary

CHANGES TO THE MAIL CLASSIFICATION SCHEDULE

The following material represents a change to the Mail Classification Schedule (MCS). The Commission uses two main conventions when making changes to the MCS. New text is underlined. Deleted text is struck through.

Part A—Market Dominant Products 1000 Competitive Product List

1600 Negotiated Service Agreements

1602 International

1602.3 Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators 1

1602.3.5 Products Included in Group (Agreements)

Each product is followed by a list of agreements included within that product.

- Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators 1

Baseline Reference

Docket Nos. MC2010-35, R2010-5 and R2010-6

PRC Order No. 549, September 30, 2010

Included Agreements

Hongkong Post–United States Postal Service Letter Post Bilateral

Agreement, ~~R2014-4~~R2015-5, expires ~~June 30, 2015~~December 31, 2016
